

External Audit: Audit Committee Briefing – June 2014
Report by Head of Finance

Summary: This report appends a Local Government Audit Committee Briefing issued by the Authority’s External Auditors, Ernst & Young.

Recommendation: That the briefing, including the key questions for Audit Committees as set out on page 11, be noted.

1 Introduction

1.1 This report appends a Local Government Audit Committee Briefing issued by the Authority’s External Auditors, Ernst & Young (EY).

1.2 The Audit Manager, David Riglar, will be attending the meeting.

2 Key Issues

2.1 This briefing is presented to Members as a “for information” item. It should be noted that it addresses wider issues affecting all local authorities and as such, some items (for example the DWP Single Fraud Investigation Service) are of less significance for the Broads Authority.

2.2 The items of relevance to the Authority are:

- The economic and sector issues update, in particular regarding service sharing and contract management (page 2 onwards);
- The update on the Future of Local Audit (page 6); and
- The key questions for the Audit Committee (page 11).

Background papers: None

Author: Titus Adam
Date of report: 20 June 2014

Broads Plan Objectives: None

Appendices: APPENDIX 1 – Ernst & Young Local Government Audit Committee Briefing (June 2014)



Local Government Audit Committee Briefing

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Introduction

This sector briefing is one of the ways that we hope to continue to support you and your organisation in an environment that is constantly changing and evolving. It covers issues which may have an impact on your organisation, the Local government sector and the audits that we undertake. The public sector audit specialists who transferred from the Audit Commission form part of EY's national Government and Public Sector (GPS) team. Their extensive public sector knowledge is now supported by the rich resource of wider expertise across EY's UK and international business. This briefing reflects this, bringing together not only technical issues relevant to the local government sector but wider matters of potential interest to you and your organisation. Links to where you can find out more on any of the articles featured can be found at the end of the briefing, as well as some examples of areas where EY can provide support to Local Authority bodies. We hope that you find the briefing informative and should this raise any issues that you would like to discuss further please do contact your local audit team.



Building a better
working world



Economic and sector issues

Economic Outlook

The ITEM Club, one of the UK's foremost independent economic forecasting groups, sponsored by EY, has published its Spring Forecast. With GDP projected to grow 2.9% this year and 2.3% in 2015, and interest rates unlikely to rise until late 2015, the outlook is for a period of 'steady as she goes', with sustained if unspectacular growth underpinned by relatively low inflation. Whilst the report highlights the concern that risks remain, it considers that the UK's economic recovery is on an increasingly firm footing.

The scenario outlined above is seen by the group to be dependent on several things, notably that consumer spending is supplemented by a rebound in business investment and exports – which official figures suggest is starting to happen. The report indicates that this would help the economy to register steady growth in output over the next few years whilst avoiding excessive rises in credit.

The ITEM Club highlights that a key challenge will be maintaining a balance between different areas of the economy, preventing each from expanding too fast or too far e.g. growing workforce keeping wage inflation under control, and the policing of mortgage lending by the FCA limiting house price rises.

DWP Single Fraud Investigation Service

The formation of a Single Fraud Investigation Service (SFIS) was announced in the Chancellor's Autumn Statement. SFIS will exist as a single organisation within DWP, and will be an element of DWP's new Fraud and Error Service. Its role will be to investigate and prosecute Social Security welfare benefits and Tax Credit fraud, bringing together investigations which are currently the remit of DWP, local authorities and HMRC, with prosecutions conducted by the Crown Prosecution Service in England and Wales. DWP has said that it will continue to work with local authorities to ensure that data is shared where permissible.

The main objectives of the scheme as cited by the DWP are:

- ▶ To operate under a single policy and set of procedures for investigating all welfare benefit fraud.
- ▶ To conduct single investigations covering all welfare benefit fraud.
- ▶ To rationalise existing investigations and prosecution policies, improving efficiency, consistency and fairness.
- ▶ To enhance closer working between DWP, HMRC and local authorities.
- ▶ To bring together the combined expertise of all three services.
- ▶ To support the fraud and error integrated strategy of preventing fraud and error in the benefit system by detecting and correcting fraud and punishing and deterring those who have committed fraud.



Economic and sector issues

Some concerns have been raised by Local Authorities and trade unions about the proposals:

UNISON has raised concerns about the proposals to transfer current local authority investigations staff into the Department – a change from the original proposal to remain employed by Local Authorities but work under DWP policies and procedures. This could affect around 790 staff.

The LGA has questioned the need to establish SFIS due to what is in their view the successful record of local authorities on addressing benefit fraud. It has also challenged whether or not SFIS would be able to achieve its stated aim of conducting single investigations covering all welfare benefit fraud, since some elements of fraud against local authority services (such as fraud against localised Council Tax Support scheme, social housing tenancies and Blue Badge disabled parking) would be considered out of scope. This is linked to the concern that by centralising housing benefit fraud investigations, local expertise will be lost.

Implementation is planned to start from October 2014, continuing until March 2016, although the Department is considering a small number of test sites beforehand. Pilots have been running since early 2013 in four local authority areas (Corby Borough Council; Glasgow City Council; London Borough of Hillingdon; Wrexham Council), with an additional pilot in Oldham covering Universal Credit which began in April 2013.

Council service sharing saves taxpayers £350mn

According to the LGA there are now 337 councils engaged in 383 shared service agreements, resulting in £357mn of efficiency savings. The total saved has increased by £83mn since last year, with the biggest increases seen in adult services and culture, leisure and tourism.

At least 95% of all English councils now share services with other local authorities and public sector bodies. Information about shared services is contained in an interactive map on the LGA's website; this map also records external collaboration for the first time. Councils can use this map to develop shared services in their own organisations.

Contracting out public services to the private sector

“Government is clearly failing to manage performance across the board, and to achieve the best for citizens out of the contracts into which they have entered.”

This is a conclusion reached by the House of Commons Committee of Public Accounts (the 'PAC') in March 2014 after the PAC took evidence from the National Audit Office and central government bodies such as the Cabinet Office and Department of Health.

Although aimed at central government, the PAC's report is a timely reminder that for many Local Government bodies, the delivery of public services is increasingly dependent on the interaction between the private and public sectors. However, as pointed out by the PAC, in order for this relationship to result in the efficient delivery of public services, the public sector needs to demonstrate its commitment to effective contract management.

The PAC made a range of recommendations in four key areas. In this briefing we consider contract management and delivery. We will consider Capability, Transparency and Ethical Standards in our next quarterly briefing.



Economic and sector issues

Contract management and delivery

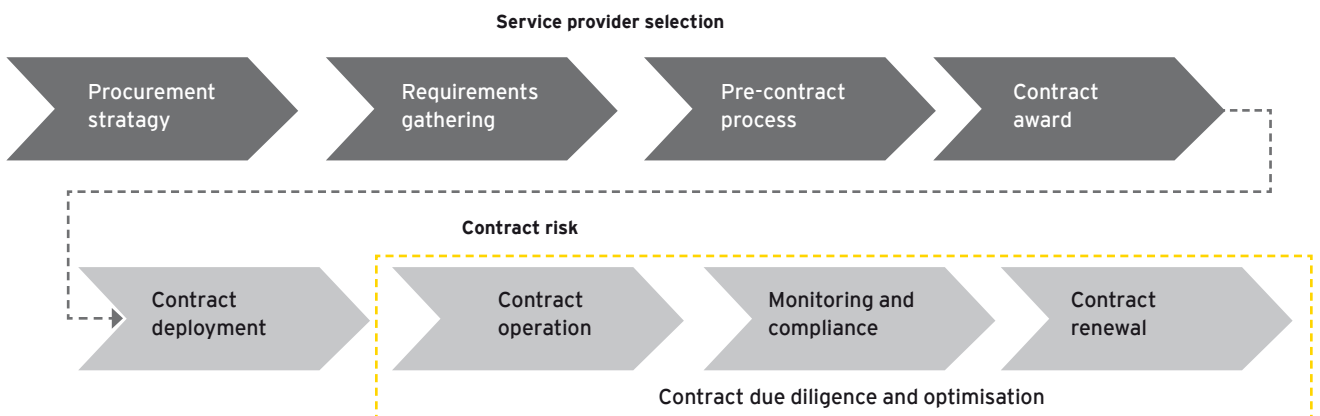
Our own experience suggests that both central and local government invest large amounts of time in selecting service providers, but relatively little time thereafter ensuring that contracts are managed effectively to deliver the intended benefits, and to manage contract risk. The diagram below illustrates the relevant phases of the overall contract process.

Critically, we often find that performance indicators are not considered in detail or agreed until after contracts have been awarded. Accordingly, there is a risk that these indicators:

- ▶ Are not effectively targeted towards the required performance objectives and/or.
- ▶ Are not subject to audit because of a lack of access rights.

Furthermore, as identified by the PAC, penalties for non-performance are not always enforced even where they are available and identified. The failure to enforce penalties only increases the likelihood of continued under-performance in the delivery of public services and the sense that the public sector does not take contract management seriously.

The PAC report therefore highlights an opportunity for Local Government bodies to both save money and increase public confidence in the use of public funds, through effective contract management.





Accounting, Auditing and Governance

Accounting for schools in local authorities

CIPFA has recently held a single issue consultation on Accounting for Schools in Local Authorities in England and Wales relating to the 2014/15 Code of Practice on Local Authority Accounting in the United Kingdom. The 2014/15 Code will apply to accounting periods starting on or after 1 April 2014. The consultation focuses largely on the application of the 2014/15 Code's provisions on primarily the Group Accounting Standards, and sets out CIPFA/LASAAC's proposals for developing an addendum for the 2014/15 Code. The Working Group has concluded that for local authority maintained schools (including community schools, voluntarily controlled, voluntary aided and foundation schools), the balance of control is with the local authority, and their transactions should therefore be included in the local authority financial statements. The Working Group has considered the practical implications and recommends that consideration is given to schools being included in the local authority single entity financial statements. The consultation closed on 4 April 2014.

Accounting for infrastructure projects within enterprise zones and tax increment financing funded programmes

The Local Authority Accounting Panel (LAAP) has issued a discussion paper on this topic to assist local authorities who are considering such schemes. There are a number of initiatives involving local authorities investing in infrastructure or other development projects on the basis that the investment will result in increased business rates yields which can be used to finance the cost. However, there is a risk that projections of incremental income may not be wholly reliable, and there are also accounting issues which may determine whether a project is viable. The local authority will need to consider the extent to which they are a principal or an agent, the accounting implications for the various vehicles in which they may acquire an interest, and the potential for a revenue deficit in the early part of the programme as costs are incurred in advance of income being receivable. The potential revenue deficit is the issue which is most likely to threaten a project's viability, as costs may be incurred in advance of new income being receivable, and councils are obliged to budget to break even each financial year.



Accounting, Auditing and Governance

A Framework for Audit Quality

The International Auditing and Assurance Standards Board (IAASB) published a report on 18 February 2014 on audit quality with the aim of generating positive discussions within organisations to improve audit quality. 'A Framework for Audit Quality – Key elements that create an environment for audit quality' sets out three key objectives:

- ▶ Raising awareness of the key elements of audit quality.
- ▶ Encouraging key stakeholders to explore ways to improve audit quality.
- ▶ Facilitating greater dialogue between key stakeholders on the topic.

The Framework recognises that there is no universally accepted definition of audit quality and has set out various factors which they consider contribute to audit quality at the engagement, audit firm and national levels. It highlights the importance of a range of contextual factors, including laws and regulations, the litigation environment, corporate governance, and the financial reporting framework, which together can impact the nature and quality of financial reporting and, directly or indirectly, audit quality.

The IAASB will maintain a focus in 2014 to encourage dialogue on audit quality.

Future of Local Audit

Following the receipt of Royal Assent by the Local Audit and Accountability Act 2014 in January 2014, approval of secondary legislation will be required in order to give effect to many of the provisions of this Act. Following a consultation on this secondary legislation, which closed in December 2013, the Government has now published its response. The consultation paper covered the following areas:

- ▶ **Smaller authorities' regulations**, including draft regulations for a specified person to appoint auditors to smaller authorities. The Government does not intend to allow smaller bodies to opt out of this regime during a contract period, nor to allow the specified person to forcibly opt out a body; authorities which exceed the £6.5mn threshold, or choose to undergo a full code audit will automatically be opted out. The Government proposes to specify a maximum contract period of five years. The consultation also set out the Government's policy intention for smaller bodies with turnover not exceeding £25,000 per annum to be exempt from routine audit. There are several circumstances where the exemption will not apply, including during the first three years after the authority is established, and authorities which qualify for the exemption may still choose to have an audit.



Accounting, Auditing and Governance

- ▶ **Auditor panel and auditor independence regulations;** the draft regulations extend the definition of an independent panel member, set out the minimum membership of an auditor panel, and apply several existing local authority enactments to panels. An audit committee can already act as an auditor panel provided it has an independent chair and majority. Several authorities may share an audit panel, and where authorities have opted in to national procurement arrangements, the Government intends that the requirement to appoint an auditor panel will not apply. This section of the consultation also covers auditor resignation and removal; which the Government expects to be a rare occurrence.
 - ▶ **Eligibility and regulations of auditors;** a local audit register will be published containing the names of those deemed competent to take primary responsibility for a local audit. An appropriate qualification will be considered necessary, but not sufficient – individuals will also need an appropriate level of competence. The draft regulations also contain thresholds defining which bodies' audits will be considered a 'major local audit' and hence subject to quality monitoring from the Financial Reporting Council's Audit Quality Review team. The Government is considering how to clarify some of the definitions in these regulations.
 - ▶ **Conduct of local audit** – the Government intends to modify the requirement for some bodies (including Port Health Authorities and Internal Drainage Boards) to consider a public interest report or recommendation within one month, to 'as soon as is practicable'.
 - ▶ **Accounts and Audit Regulations;** this section of the consultation covered the provisions for financial management, internal control and internal audit, as well as the process for preparing and approving the statement of accounts. Comments were also invited on bringing forward the timetable for local government audit, and on changes to the framework for the exercise of public rights of inspection and objection. The Government intends to keep public inspection rights, but to address the issues surrounding low take-up of these rights in the draft regulations proposed for consultation in May 2014.
- The Government plans to amend the draft regulations in line with the responses noted above and to issue a further consultation in May 2014 covering further regulations associated with smaller authorities, regulations to allow for the establishment of a sector-led body to procure and appoint local auditors, and Accounts and Audit regulations. The intention is that these regulations will be laid before Parliament later this year.



Regulation News

Role of the Chief Finance Officer in the Local Government Pension Scheme

CIPFA has issued a consultation draft on the role of the CFO in the Local Government Pension Scheme (LGPS), as a supplement to the statement on the role of the CFO in Local Government. The statement sets out five principles, including a summary, shown below. The supplement on the LGPS sets each of these principles in the context of the financial management of the LGPS, which highlight the importance of the role of the CFO in relation to the LGPS.

The CFO in a public service organisation:

- ▶ Is a key member of the Leadership Team, helping it to develop and implement strategy and to resource and deliver the organisation's strategic objectives sustainably and in the public interest.
- ▶ Must be actively involved in, and able to bring influence to bear on, all material business decisions to ensure immediate and longer term implications, opportunities and risks are fully considered, and alignment with the organisation's financial strategy.
- ▶ Must lead the promotion and delivery by the whole organisation of good financial management so that public money is safeguarded at all times and used appropriately, economically, efficiently and effectively.

To deliver these responsibilities the CFO:

- ▶ Must lead and direct a finance function that is resourced to be fit for purpose.
- ▶ Must be professionally qualified and suitably experienced.

Future of NFI and counter fraud following the closure of the Audit Commission

The Audit Commission's National Fraud Initiative matches data from 1,300 public sector and 77 private sector organisations. The outcomes since 1996 include the prevention and detection of pension overpayments, council tax single person discounts incorrectly awarded, and housing benefit overpayments, together worth over £860mn. Following the closure of the Audit Commission in March 2015, the NFI will transfer to the Cabinet Office.

The Chartered Institute of Public Finance and Accountancy (CIPFA) will also take on some of the Audit Commission's counter fraud roles. The counter-fraud function currently undertaken by the Commission will transfer to a new public sector 'Counter Fraud Centre', which will be established by CIPFA. Existing counter-fraud work undertaken by the Commission includes the annual 'Protecting the Public Purse' report, tailored fraud briefings for local authorities, and the survey of fraud and corruption in England. The new Centre will build on this existing work and



Regulation news

introduce new practical guidance for tackling fraud and corruption. Although CIPFA will not have the same statutory powers as the Commission, it intends to continue the annual comprehensive survey of fraud and corruption, as well as expanding the Counter Fraud Centre's reach beyond local government.

Government consultation on flexibility in the use of capital receipts

Between July and September 2013, the Government ran a consultation on allowing capital receipts from new asset sales to be used for one-off revenue purposes. The results of this consultation have now been published. The aims of the proposal were to encourage good asset management planning, and to enable additional resources from asset sales to give flexibility for reforming, integrating or restructuring services. The response to the consultation was clearly positive, so as part of the Autumn Statement the Government announced that they will allow some flexibility for local authorities to use £200mn of receipts from asset sales across 2015/16 and 2016/17 to fund one-off costs of service reforms. Authorities will have to bid for a share of this allowance, and permission for flexible use of capital receipts will be through a capitalisation direction from the Secretary of State under section 16(2)(b) of the Local Government Act. Capital receipts obtained prior to the issue of this consultation will not be allowed to be used for this purpose as one aim of the policy is to encourage new asset sales. As part of the bid process, local authorities will need to assess the extent to which the asset sales are additional to sales which would have occurred anyway.

Consultation on the process for setting up a new town/parish council

The Government ran a consultation ending in May 2014 on a proposal to make it easier to set up a new town or parish council. The proposed new measures are intended ease the process by reducing the burden from the current Community Governance Review process. The current process requires either the Local Authority to carry out a review, or the local community petitioning the Local Authority to create a new parish council, as part of which process the petitioner must also propose the boundaries of the new parish. A minimum number of signatories to the petition are required, depending on the size of the neighbourhood area in question, and the high number required can be a barrier to local campaigns. The current process is also relatively slow, as the required twelve month timescale does not include time for the Local Authority to carry out preparatory work. The proposed new measures include lowering the thresholds of signatures required, shortening the amount of time the Local Authority can take to carry out a Community Governance Review, and allow Neighbourhood Forums to trigger a Community Governance Review.

Audits in 2014/15: work programme and scale fees

Following consultation, the Audit Commission has confirmed the work programme and fee scales for the audit of the accounts for 2014/15 for local government, fire, police and health bodies (including CCGs). The scale fee for individual Local Government bodies is available on the Audit Commission website.



Regulation news

The Audit Commission expects to close on 31 March 2015, as a result of the provisions of the Local Audit and Accountability Act 2014. It will set the fees and work programme for 2015/16, which will be the first year of audit following their closure. The responsibility for overseeing the audit contracts of nearly 11,000 public organisations, spanning local authorities, police, health, fire bodies and rescue services, and for setting fees under them, will pass to a transitional body from April 2015. Ministers have announced that this body will be an independent private company to be set up by the Local Government Association. It will also have responsibility for the Value for Money Profiles tool. The Commission's current contracts with audit suppliers will run until 2016/17, with a possibility of extension up to 2020. Following this, audited bodies will be able to appoint their own auditors.

Award of Audit Contracts

Prior to the decision to abolish the Audit Commission's audit practice, approximately 30% of local public audits were carried out by private sector audit firms. In April 2013 the Audit Commission announced that it would be retendering these contracts which had been awarded in 2006 and 2007.

Following a competitive tendering process, the Audit Commission confirmed the award of two year contracts to:

- ▶ BDO LLP, to the value of £4.6mn a year, covering audits in the South.
- ▶ EY LLP, to the value of £9.6mn a year, covering audits in the North and the South.
- ▶ KPMG LLP, to the value of £9.6mn a year, covering audits in the North and the South.

There will now be a consultation with the audited bodies concerned on the appointment of auditors, prior to putting the appointments to the Audit Commission Board for approval in December 2014.



Key Questions for the Audit Committee

What questions should the Audit Committee be asking itself?

Following client feedback we have introduced a section which draws together some of the key messages from the briefing for consideration by Audit Committee members:

- ▶ What impact will the introduction of the SFIS have on our capacity and expertise to tackle other areas of fraud risk, such as council tax, business rates, housing and other corporate fraud?
- ▶ Is there scope for us to take advantage of further opportunities for efficiency savings resulting from joint working with other public sector bodies?
- ▶ Where joint working arrangements are already in place, are they still fit for purpose or do we need to consider modifying the arrangements in line with our changing challenges and priorities?
- ▶ What level of governance does our organisation have around contract management and delivery with both our public and private sector partners?
- ▶ How can we work with our audit engagement team to improve audit quality?



Find out more

Economic Outlook

For the full analysis go to:

<http://www.ey.com/UK/en/Issues/Business-environment/Financial-markets-and-economy/Economic-Outlook>

DWP Single Fraud Investigation Service

Read more about the proposals at:

<https://www.gov.uk/government/collections/single-fraud-investigation-service>

Council service sharing saves taxpayers £350mn

Find out more at <http://www.local.gov.uk/shared-services-map>

Contracting out public services to the private sector Read the NAO report at:

<http://www.nao.org.uk/wp-content/uploads/2013/11/10296-001-BOOK-ES.pdf>

To find out how EY can help with contract management, contact a member of your engagement team.

Accounting for schools in local authorities

The consultation has now closed, however, you can view the details at:

<http://www.cipfa.org/SingleIssueITCAccountingforSchoolsinLocalAuthorities>

Accounting for Infrastructure Projects within Enterprise Zones and Tax Increment Financing Funded Programmes

Read more at:

<http://www.cipfa.org/-/media/files/policy%20and%20guidance/panels/local%20authority%20accounting%20panel/accountingforenterprisезones.pdf>

A Framework for Audit Quality

The publication can be found in the 'Focus on Audit Quality' section of the IAASB's website:

<https://www.ifac.org/auditing-assurance/focus-audit-quality>

Future of Local Audit

Find out more at:

<https://www.gov.uk/government/consultations/future-of-local-audit-consultation-on-secondary-legislation>

Role of the Chief Finance Officer in the Local Government Pension Scheme

Find out more at:

<http://www.cipfa.org/-/media/files/policy%20and%20guidance/consultations/140211role%20of%20the%20chief%20finance%20officer%20in%20the%20lgpsconsultation%20draft.pdf>



Find out more

Future of NFI and counter fraud following the closure of the Audit Commission

Further information is available at:

<http://www.audit-commission.gov.uk/2014/03/commissions-national-counter-fraud-function-will-go-to-safe-hands/>

Government consultation on flexibility in the use of capital receipts

Details of the response to the Government's consultation are available at:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/300060/Proposals_for_the_use_of_capital_receipts_from_asset_sales_to_invest_in_reforming_services_-_response_to_consultation.pdf

Consultation on the process for setting up a new town / parish council

Details of the consultation are available at:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/297813/Consultation_on_a_proposal_to_use_a_Legislative_Reform_Order_for_making_it_easier_to_set_up_a_town_and_parish_council.pdf

Audits in 2014/15: work programme and scale fees

The scale fees are published at:

<http://www.audit-commission.gov.uk/audit-regime/audit-fees/201415-work-programme-and-scales-of-fees/>

Award of Audit Contracts

Read the Audit Commission press release at:

<http://www.audit-commission.gov.uk/2014/03/the-audit-commissions-legacy-includes-a-further-25-per-cent-reduction-in-annual-audit-fees/>

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